BEFORE THE NEBRASKA PUBLIC SERVICE COMMISSION

In the Matter of the Nebraska Public Service Commission on its own motion to conduct an investigation on intrastate switched access charge policies and regulation codified in Neb. Rev. Stat. Section 86-140.	Application No. C-4145/NUSF-74/PI-147

COMMENTS OF UNITED TELEPHONE COMPANY OF THE WEST d/b/a EMBARQ

On February 24, 2009 the Nebraska Public Service Commission ("Commission") opened the above-referenced docket to establish the minimum evidence required when a carrier seeks access rate changes under Neb. Rev. Stat. Section 86-140. The Commission also wishes to evaluate its access charge policies and goals and determine whether those policies and goals should be modified. United Telephone Company of the West d/b/a Embarq ("Embarq") appreciates the opportunity to provide comments on these important issues.

MINIMUM REQUIRED EVIDENCE

The Commission seeks to clarify the minimum objective evidentiary criteria that should be required of local exchange companies ("LECs")[1] voluntarily seeking to increase access rates to allow the Commission to make a finding that the proposed rates are just and reasonable. In general, Embarq believes that a company bringing action before the Commission bears the burden of production and the burden of proof. The

[1] It is believed that "LECs" is intended to refer to both incumbent LECs and competitive LECs.

risk of not satisfying the burden of production and the ultimate burden of proof rests with the party seeking a change in rates. Therefore, any LEC (either incumbent or competitive) that seeks to voluntarily increase its access rates should produce documents and sufficient evidence demonstrating that the proposed increases in switched access rates are just and reasonable. Clearly, delivering at least some evidence supporting the rate increase would seem, at first blush, to be advisable. However, the circumstances surrounding any request to increase access rates will vary for each carrier and for each filing. And it is difficult to identify precise documentation that the Commission will need to review to make this determination in all situations. The Commission should therefore not limit a carrier's ability to provide relevant and applicable information through a prescribed list of required documentation.

Embarq recommends that the Commission should not create a list of required documentation, as the Commission may find that its "required" documentation is obsolete or of little use. Rather, the Commission should require, at a minimum, two measures: 1) To the extent the Commission determines a list of minimum required information, the list should not preclude parties from introducing additional information that is just, reasonable and relevant to their circumstances; and 2) The Commission should permit LECs voluntarily requesting an access rate increase to work with Commission Staff to determine what additional documents should be provided to support the justness and reasonableness of the proposed rates for that particular

situation. Such documentation may include a forward-looking total cost of service study, trends in access lines and access minutes of use, federal and state universal service support, and universal service obligations.[2] Access line loss due to competition and local market conditions may also be useful to the Commission during its review. The Commission may request additional documentation, if it deems necessary, and the LEC may need to supplement, as may be necessary.

The Commission made several suggestions regarding the minimum objective evidentiary criteria and requested comments on those suggestions. Embarq respectfully provides the following comments:

1. **The NUSF-EARN form compiled on a supported services basis as a tool to measure the cost of providing access in conjunction with supported services.**

While the Commission has found that a full cost study is not required when a LEC voluntarily seeks an intrastate switched access rate increase,[3] Embarq believes that a forward-looking total cost of service study is the best approach to evaluate the proper level of support. Parties should not be precluded through a minimum evidentiary requirement from presenting relevant and important information that would aid in the development of a full record and the Commission's evaluation of the requested rate increase. Although historical information can provide support for forward-looking

[2] To the extent a LEC does not provide the foregoing information with its filing, and so long as the LEC is not precluded from presenting supplemental information, the Commission can request the LEC to provide the NUSF-EARN and/or the Annual Report Form M as a minimum level of support.

[3] *See In the Matter of the Nebraska Public Service Commission to conduct an investigation of Qwest Corporation's Proposed Switched Access Charge Rates,* Application No. C-3945/NUSF-60.02/PI-138, Order issued February 3, 2009, page 10.

information, the question of the proper level of a LEC's intrastate switched access rates is forward-looking and should be answered based upon forward-looking information.

Should the Commission choose not to adopt a forward-looking total cost of service study, Embarq believes that a carrier's NUSF-EARN form can provide some information regarding a carrier's historical earnings. However, historical information will not provide the Commission with answers regarding future costs or revenue needs. The NUSF-EARN form can only provide the Commission with an idea of where a company's historical earnings fall relative to the 12% earnings cap for NUSF support. Embarq notes, however, that not all carriers are required to file the NUSF-EARN form; therefore, the Commission will need to determine the documentation that should be required for those carriers that do not file the NUSF-EARN form.

2. **The NUSF-EARN form to consider the federal and state universal service support received by the requesting carrier.**

Federal and state universal service support, local exchange rates, and access rates are inextricably linked, all working together and allowing a LEC to appropriately recover its costs of providing universal service at affordable rates to retail end users. A change in the revenues received from one source will likely impact the need for revenues from the other sources.

The Commission acknowledged the relationship between local exchange rates, intrastate access rates, and federal and state universal service support when it adopted the revenue benchmark calculations as part of the Nebraska Universal Service Fund

("NUSF") Support Allocation Methodology which determines a carrier's state universal service support. The revenue benchmark for each company is calculated based on the benchmark local exchange rates, the federal subscriber line charge, and a contribution from intrastate access, among other things. The Commission also imputes federal universal service support in the NUSF-EARN form, which also helps determine a carrier's state universal service support. Because federal and state universal service support, as well as access rates, are important components to the determination of universal service and the affordability of local exchange rates in Nebraska, a LEC's support from these programs should be considered during the process of evaluating the need for an access rate increase.

In addition to considering current federal and state universal fund support, the Commission should also consider if universal service support has increased or decreased in the past, and the expected changes in support going forward. Given the history in Nebraska and the NUSF, information on federal and state universal service support is generally publicly available and can be obtained from a number of sources.

3. Alternative revenue generation sources for the carrier, including local rates in both urban and rural areas.

The Commission's prime objective when evaluating a request to increase access rates should be to ensure that all Nebraskans have access to telecommunications services at reasonably comparable and affordable rates. As the Commission is well aware, and as Embarq noted above, intrastate access rates and the federal and state

universal service fund in Nebraska are inextricably linked with local service rates and play vital roles in ensuring that local exchange rates remain affordable.

Neb. Rev. Stat. Section 86-323 states that "[q]uality telecommunications and information services should be available at just, reasonable, and affordable rates"[4] and that "[t]he implicit support mechanisms in intrastate access rates throughout the state may be replaced while ensuring that local service rates in all areas of the state remain affordable."[5] Affordability clearly is the key issue in Nebraska's statutory scheme. The Commission also has previously found that "affordable access to telecommunications and information services at comparable rates is key to developing a long-term universal service mechanism."[6] More recently, this Commission, in its comments to the Federal Communications Commission ("FCC") in intercarrier compensation reform, stated,

> The primary goal is to preserve and advance universal service for the consumers' benefit and to offer affordable and reasonably comparable rates and services to consumers in rural areas of the state. Notwithstanding the primary goal of affordable rates, Nebraska consumers have basic local rates which are at the high end of the national affordability benchmark.[7]

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[4] Neb. Rev. Stat. Section 86-323(1).

[5] Neb. Rev. Stat. Section 86-323(7).

[6] *See In the Matter of the Nebraska Public Service Commission, on its own motion, seeking to establish a long-term universal service funding mechanism,* Application No. NUSF-26, Findings and Conclusions entered November 3, 2004, paragraph 9.

[7] *See In the Matter of High-Cost Universal Support, Federal-State Joint Board on Universal Service, Lifeline and Link-Up, Universal Service Contribution Methodology, Numbering Resource Optimization, Implementation of the Local Competition Provision in the Telecommunications Act of 1996, Developing a Unified Intercarrier Compensation Regime, Intercarrier Compensation for ISP-Bound Traffic, IP-Enabled Services,* Docket Nos. WC 05-337, CC 96-45, WC 03-109, WC 06-122, CC 99-200, CC 96-98, CC 01-92, CC 99-68, WC 04-36, Comments of the Nebraska Public Service Commission filed November 26, 2008, page 9.

Achievement of the state's statutory requirements[8] to ensure universal access to telecommunications service and reduce or eliminate implicit subsidies in intrastate access rates cannot be accomplished without sufficient explicit funding. Doing so in this era of vigorous and growing competition creates an unfunded mandate and may initiate a vicious circle of rate increases and access line disconnections that will ultimately harm both the end user and the incumbent local exchange carrier ("ILEC"), or the ILEC will work within the pricing constraints of competitive markets in an attempt to hold customers. In either event, the ILEC's financial condition will rapidly deteriorate and it will ultimately be unable to fulfill its universal service obligations.

As noted above, the Commission already acknowledges that the Nebraska end user is paying at the high end of the national affordability benchmark. Increasing local exchange rates will encourage more end users to "cut the cord" and rely exclusively on wireless or VoIP service for their telecommunications needs. Moreover, ILECs as carriers of last resort are obligated to provide service to any customer within its service territory that requests it, no matter the cost. As more customers opt to purchase their telecommunications services from other providers, the ILEC will be forced to recover the cost of providing service over fewer customers, requiring yet more rate increases and/or likely reductions in service quality. If the ILEC continues to increase local exchange rates, it may find that it has priced itself out of much of the market, ultimately

[8] *See* Neb. Rev. Stat. Section 86-323.

providing service only to those high cost customers that cannot receive service from one of the lower priced competitors. Because an ILEC's competitors can choose which customers to serve (and they choose to serve only the least cost customers), the ILEC will find itself in the position of serving only high cost customers, with little or no subsidy from customers in low cost areas to help offset its costs of providing universal service throughout its service territory. Unless additional federal or state universal service support becomes available, the subsidies in intrastate switched access rates are critical to recovery of costs, particularly for ILECs serving high-cost, rural areas of the state.

Performance of the universal service obligation is contingent upon funding. In competitive markets, implicit subsidies quickly erode, making explicit subsidies even more important. The universal service obligation must be fully funded, or it should be reduced or eliminated. Lack of funding will cause an upward pressure on local rates and increase the risk that LECs may not be able to meet their universal service obligations or continue to provide high-quality service. LECs stand ready to serve "all", but if funding for this social obligation is not provided, the obligation must be removed. This is a matter of basic fairness.

Competition plays a major role in determining an ILEC's local exchange rates and competition in the telecommunications market in Nebraska is robust. The Commission has determined that ILECs may charge residential local exchange rates of

between $17.50 and $19.95 without losing NUSF support.[9] However, as competition increasingly constrains price levels, market forces may not permit residential local exchange rates to increase much above $17.50, if at all.[10] Simply put, ILECs serving high-cost, rural areas of the state cannot *both* price at competitive levels and price to recover its costs. Therefore, while the Commission may have provided ILECs with pricing flexibility for local exchange services, pricing flexibility is only a potential opportunity and only a small part of the solution. Pricing flexibility is not a viable means of ensuring universal service at affordable rates in the state of Nebraska when an ILEC is serving high cost rural areas in a competitive environment. An explicit, sufficient fund is required.

In summary, the Commission must ensure that local exchange rates remain affordable. The Commission cannot assume that an ILEC can recover some or all of a needed revenue increase through local rate increases and/or through the illusion of pricing flexibility, because competitive markets do not allow it. Thus, an ILEC – particularly one serving high cost, less dense areas – may need to increase intrastate access rates or receive additional support from the state universal service fund. As

[9] *See In the Matter of the Nebraska Public Service Commission, on its own motion, to make adjustments to the universal service fund mechanism established in NUSF-26,* Application No. NUSF-50, Order issued December 19, 2006, Paragraph 32.

[10] Since the Commission issued its order in NUSF-50 in December 2006, only Great Plains Communications, Inc. has increased R1 rates above the previous $17.50 benchmark rate, to $19.20. Elsie Communications, Inc. and Dalton Telephone Company are in the process of increasing their R1 rates to $19.25. Qwest had previously increased its R1 rate to $18.15 in 2005. The fact that the majority of ILECs have not implemented residential local exchange rate increases (despite losing NUSF support which assumes the rates of $17.95 in urban areas and $19.95 in rural areas) is indicative of the competitive marketplace and the limited ability of ILECs to increase local rates.

illustrated above, federal or state universal service funding becomes critical in a competitive environment to ensure universal service at affordable rates. If the Commission chooses to not sufficiently fund the universal service obligation, carriers must be relieved of it.

4. **Establish a reasonable rate-of-return figure for carriers seeking access rate increases along with establishing an appropriate test year.**

Embarq urges the Commission not to establish a rate-of-return and test year for any carrier seeking access rate changes. Doing so brings the Commission dangerously close to rate-of-return ratemaking, to which most Nebraska ILECs are not subject.[11] Currently, ILECs not subject to rate regulation are not subject to rate case requirements such as determining an appropriate rate of return or test year when requesting an increase to local exchange rates. The Commission should not create a situation whereby an ILEC may become subject to rate-of-return ratemaking for intrastate switched access rates, particularly when the ILEC's competitors likely would not be subject to similar restrictions.

5. **Examine the minutes of use (MOU) demand and access line counts of the carrier, consistent with a specific test year.**

Information regarding access line counts and MOUs demand can be beneficial to the Commission as part of its review of intrastate access rate changes. However, access

[11] Neb. Rev. Stat. Section 86-139.

line counts and MOUs demand for a specific test year will not provide the Commission with the complete picture.

ILECs have been experiencing declines in access line counts and MOUs for a number of years, a trend that is likely to continue for the foreseeable future as competition continues to erode ILEC market share. The ILEC telecommunications network is capital intensive and experiences high fixed costs. As a result, per unit costs increase as access lines are lost. Information regarding access line counts and MOUs demand can begin to provide the Commission with valuable insight into issues such as the demand for the carrier's services, the level of competition the carrier is experiencing, and the carrier's ability to recover needed revenue increases from either local exchange rates or intrastate access rates. Embarq recommends the Commission review trends in access line counts and minutes of use over a number of years as part of any request to adjust intrastate access rates.

INTRASTATE ACCESS POLICY OBJECTIVES

In general, Embarq believes that the Commission's intrastate access policy goals and objectives are effective and changes should not be made at this time. The Commission has largely accomplished the goals it set in 1999, namely to reduce implicit subsidies and to help foster competition in the local exchange market. Should the Commission consider changes to its intrastate access policy goals and objectives, it should not make changes to these policies in a vacuum. Any change to the Commission's intrastate access policies will impact local exchange rates, ILEC market share, and related retail revenues, and the NUSF as well. Changes that result in insufficient funding of the universal service obligation must come with reduced or eliminated universal service obligations. Finally, any actions on the part of the FCC in pending intercarrier compensation and federal universal service support proceedings will impact Nebraska consumers and telecommunications carriers. Embarq urges the Commission to take the time to first thoroughly and deliberately review the impact from any proposed FCC or federal changes before taking action.

In response to the Commission's specific questions, Embarq provides the following:

1. **Should limits be placed on the frequency of access cases that any carrier can file with the Commission?**

Embarq appreciates the Commission's interest in limiting the frequency of intrastate switched access cases, but believes that arbitrarily imposing a limit on the

frequency of such access cases may ultimately harm both the carriers and end users. Under normal circumstances, carriers should allow approved intrastate switched access rate changes to be in effect for a sufficient period to determine the long-term impact to revenues before contemplating another rate change. However, changes in market conditions, individual facts, or federal and state policies or regulations may necessitate more frequent changes. Embarq suggests that the Commission not implement a condition limiting the frequency of intrastate switched access cases.

2. **How are access rates structured and does the structure vary from carrier to carrier? Should the structure of access rates affect the Commission's analysis of access rate increases?**

The Commission undertook significant access reform a decade ago. At that time, most companies significantly altered their access rate structures. The Carrier Common Line charge was eliminated and many companies eliminated the interconnection charge and restructured local transport charges. Generally, how a carrier structures its access rates has no impact on the Commission's analysis.

3. **Are the Commission's initial policy goals set out in 1999 for intrastate switched access reform still valid today? Have they been achieved? What further steps, if any, should be considered?**

The Commission's initial policy goals for intrastate access reform and the NUSF have largely been achieved. Implicit subsidies in intrastate access rates have been reduced and replaced with explicit subsidies from the NUSF and increases to local exchange rates. However, competition in the local marketplace has significantly

increased from CLECs, VoIP providers, and wireless carriers, eroding vast amounts of support from other services. This erosion requires an increasing reliance on explicit support in order for ILECs to continue to meet universal service obligations and to comply with carrier of last resort obligations in all areas of its service territory. Accordingly, the need for and the importance of a properly sized and fully operational NUSF continues to be necessary.

Should the Commission consider changes to the intrastate access charge structure and policies and, by default, to the NUSF, Embarq cautions the Commission from acting too quickly to make any changes that might further erode explicit subsidies as well as implicit subsidies in intrastate switched access rates. The FCC currently has proceedings underway to review intercarrier compensation and the federal universal service funding mechanism, and it likely will make significant changes to both soon, impacting Nebraska universal service funding, intrastate access rates, and local exchange rates. Verizon's Executive Vice President Thomas J. Tauke very recently stated:

> The FCC is ready to act on intercarrier-compensation reform. Last year the industry spent months briefing these issues and engaging in a productive and meaningful dialogue on reform. Congress should provide the FCC with a deadline to reform the intercarrier-compensation system.[12]

[12] Prepared Testimony of Verizon Executive Vice President Thomas J. Tauke, U.S. House of Representatives Committee on Energy and Commerce, Subcommittee on Communications, Technology, and the Internet "Universal Service Fund Reform" dated March 12, 2009, at 11.

It would be unreasonable, unproductive, and impractical for the Commission to consider changes to intrastate access policies until the FCC has acted on intercarrier compensation issues. Any action taken by the FCC will impact Nebraska ILECs, intrastate universal service funding and the local exchange rates paid by Nebraska consumers. As noted earlier, Nebraska ILECs have already implemented substantial intrastate access reform. Their consumers have already absorbed substantial local service rate increases. If the Commission continues to act on the forefront of intrastate access reform, a laudable goal in isolation, Nebraska ILECs and consumers will be at risk of receiving no credit for such early state reform, and may face additional rate increases with little benefit from increased federal funding.

Valuable Commission resources should not be needlessly spent developing a potentially inadequate and inapplicable record in an effort to arrive at a result that is apt to be premature at best and detrimental to Nebraska ratepayers at worst. Waiting until the FCC acts will allow the Commission to quantify the impacts changes at the federal level will have and aid in the establishment of appropriate policy going forward. For these reasons, Embarq recommends the Commission delay any efforts to modify the intrastate access charge structure or policies until the FCC is further along in its intercarrier compensation proceeding and the Commission can be sure that its actions do not inadvertently harm the Nebraska consumer.

4. **Should the Commission's policy of intrastate switched access rate reform be modified? If so, in what way?**

This Commission has been a leader in the nation on the issues of intrastate access reform and state universal service issues, and Nebraska consumers have benefitted from the Commission's actions. The Commission understands that a necessary component of access reform is universal service funding and has created a universal service funding mechanism that directs funding to the highest cost areas of the state. Therefore, any discussion of access reform changes must include the NUSF and the continued recovery of any implicit subsidies from intrastate switched access rates, unless additional funding for the NUSF is made available. As noted in its comments to question #3 above, Embarq believes that the Commission should not undertake any modifications to intrastate switched access reform until the FCC has had time to act on intercarrier compensation and federal universal service reforms. Any changes that the FCC makes will impact Nebraska intrastate switched access rates, federal universal service support, state universal support, and local exchange rates. While this Commission has been on the leading edge nationally of intrastate switched access reform and universal service funding issues, to the benefit of consumers and telecommunications companies alike, acting too quickly now may cause future harm to those same consumers and carriers.

SUMMARY

The Commission is appropriately concerned about access rate changes and access reform. It is a question that is on most regulators' minds, including those of the

FCC. For companies voluntarily seeking to increase intrastate access rates, Embarq believes that the Commission should not create a list of required documentation that should be provided as part of any such application. The circumstances behind a request to increase access rates will vary from carrier to carrier. Requiring all carriers to provide specific documentation that will supposedly support the application may end up being of little use. Embarq suggests the Commission allow carriers requesting an access rate increase to work with Commission Staff to determine the documentation that should be provided, dependent on the circumstances surrounding that case.

With respect to access reform policies, Embarq suggests that the Commission not move forward with any changes to its access reform policies at this time. The policies currently in place have been successful. In addition, actions on the part of the FCC may forestall any efforts by the Commission to make meaningful changes to access reform policies. The Commission should wait until the FCC has acted in its intercarrier compensation and universal service reform proceedings before moving forward with any potential changes to its access reform and NUSF policies. To do otherwise would risk harming the Nebraska consumer.

Respectfully submitted this 23rd day of April 2009.

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